

## **REPORT OF THE AUDITOR-GENERAL TO THE LIMPOPO PROVINCIAL LEGISLATURE AND THE COUNCIL ON GREATER LETABA MUNICIPALITY**

### **REPORT ON THE FINANCIAL STATEMENTS**

#### **Introduction**

1. I have audited the accompanying financial statements of the Greater Letaba Municipality, which comprise the statement of financial position as at 30 June 2011, and the statement of financial performance, statement of changes in net assets and statement of cash flows for the year then ended a summary of significant accounting policies and other explanatory information, and the accounting officer's report , as set out on pages ... to ...

#### **Accounting officer's responsibility for the financial statements**

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA), and for such internal control as management determines necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

#### **Auditor-General's responsibility**

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996) and, section 4 of the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of MFMA, my responsibility is to express an opinion on these financial statements based on my audit.
4. I conducted my audit in accordance with International Standards on Auditing and General Notice 1111 of 2010 issued in Government Gazette 33872 of 15 December 2010. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
5. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
6. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my adverse audit opinion.

## **Basis for an adverse opinion**

### **Investments**

7. Included in current investments of R7 029 615 as disclosed in note 9 to the financial statements, is a non current investment amounting to R6 957 958. Had this investment been recognised as a non current investment, current investments would have been stated at R71 657 and non - current investments would have increased by R6 957 958.

### **Unauthorised, irregular and fruitless and wasteful expenditure**

8. Section 62(1) (d) of the MFMA requires the accounting officer to take all reasonable steps to ensure that unauthorised, irregular and fruitless and wasteful expenditure is prevented. The municipality procured goods and services amounting to R13 789 568 in contravention of the supply chain management requirements. The amount was not disclosed as irregular expenditure in the notes to the financial statements, resulting in irregular expenditure being understated by R13 789 568.
9. The municipality procured a mayoral chain amounting to R195 000, that was not budgeted for in the annual budget approved by council. The amount was not disclosed as unauthorised expenditure in the notes to the financial statements, resulting in unauthorised expenditure being understated by R195 000.
10. The municipality incurred fruitless and wasteful expenditure amounting to R15 849 due to interest arising from late payment of supplier invoices and overpayment of home owner's allowances to employees. The amount was not included in fruitless and wasteful expenditure, disclosed in note 38 to the financial statements, resulting in fruitless and wasteful expenditure being understated by R15 849.

### **Property, Plant and Equipment**

11. I was unable to verify the existence and completeness of infrastructure assets stated at R112 808 597 in the financial statements due to inadequate descriptions and locations of the assets. Infrastructure assets had multiple asset numbers.
12. Depreciation and amortisation stated at R11 923 577 as disclosed in note 24 to the financial statements does not agree to the amount of R13 243 382 as per the assets register. Consequently depreciation and amortisation is understated by R1 319 804 and accumulated surplus is overstated by the same amount.
13. Additions to property, plant and equipment stated at R25 902 188, as disclosed in note 7 to the financial statements, does not agree to the balance of R35 598 800 as per the general ledger. Consequently property, plant and equipment is overstated by R9 696 612.
14. Standards of *Generally Recognised Accounting Practice, GRAP 3, Accounting policies, changes in accounting estimates and errors* requires that material prior period errors be corrected retrospectively in the first set of financial statements authorised for issue after their discovery by restating the comparative amounts for the prior periods presented in

which the error occurred. During the year, the municipality revised the useful lives of assets that were fully depreciated and excess accumulated depreciation amounting to R1 319 804 was written back to accumulated depreciation as per note 7 to the financial statement. Had the adjustments per GRAP 3 been applied, prior period accumulated depreciation would have decreased by R1 319 804 and accumulated surplus would have increased by the same amount.

15. Standards of *Generally Recognised Accounting Practice*, *GRAP 3, Accounting policies, changes in accounting estimates and errors* requires that material prior period errors be corrected retrospectively in the first set of financial statements authorised for issue after their discovery by restating the comparative amounts for the prior periods presented in which the error occurred. Assets amounting to R2 410 016 were omitted from the asset register of prior years and were recognised for the first time during the current year. These assets were all recognised as current year additions in the assets register with an acquisition date of 30 June 2011. Consequently current year additions are overstated by R2 410 016, and property, plant and equipment comparative figure is understated by the same amount. I was unable to determine the impact of this error on prior year accumulated depreciation and accumulated surplus due to lack of information in the assets register to allow for the re-computation of prior year accumulated depreciation. Prior year accumulated depreciation and accumulated surplus are misstated by an unknown amount.

#### **Defined benefit plans**

16. The South African Statement of *Generally Accepted Accounting Practice*, *IAS 19, Employee Benefits* requires that current service costs, interest costs and actuarial gains and losses on defined benefit plans be recognised in profit and loss. Current service costs, interest costs and actuarial gains and losses amounting to R1 239 867 as per actuarial reports, prepared by an independent actuary were not included in profit and loss for the year. Consequently, employee related costs are understated by R1 239 867 and accumulated surplus is overstated by the same amount.

#### **Accumulated surplus**

17. Accumulated surplus balance as per the statement of changes in net assets of R222 248 977, does not agree to the balance as per general ledger of R204 181 679. The entity did not reconcile the difference of R18 067 298 between the financial statements and the underlying accounting records. Consequently accumulated surplus is overstated by R18 067 298.

#### **Accounts receivables**

18. I was unable verify the valuation of accounts receivables stated at R7 576 061 in the financial statements due to the following:
  - The accounts receivables balance of R45 051 009 as disclosed in note 3 to the financial statements does not agree to the schedule used for the computation of the provision for doubtful debts by R16 232 746. Receivables as per the schedule amount to R61 961 165.

- The current year provision for doubtful debts balance of R37 474 945 as per note 3 to the financial statements differ to the amount on the supporting schedule by R16 095 887. Provision for doubtful debts as per the schedule amount to R53 570 805.
- The prior year provision for doubtful debts balance of R32 900 639 as per note 3 to the financial statements differ to the amount on the current year supporting schedule by R9 837 553. Prior year provision for doubtful debts as per the schedule amount to R42 738 192.
- Increase in provision for doubtful debts of R4 960 466 as per the statement of financial performance, differ to the amount of R10 832 613, as per note 3 and the schedule used for the computation of the provision for doubtful debts. Consequently increase in provision for doubtful debts in the statement of financial performance is understated by R5 872 147 and accumulated surplus is overstated by the same amount.
- The South African Statement of *Generally Accepted Accounting Practice, IAS 39, Financial instruments: recognition and measurement* requires an entity to assess at the end of each reporting period whether there is any objective evidence that a financial asset or group of financial assets are impaired. The provision for doubtful debts include debts owed by government departments, public entities and municipalities amounting to R4 014 512. The municipality did not assess whether there was objective evidence that receivables are impaired. The municipality provided for impairment on all debtors who did not pay their debts in the last 12 months. The municipality did not take into account different categories of debtors.

19. I was unable to satisfy myself as to the existence, valuation and completeness of other consumer debtors stated at R15 066 559 in note 3 to the financial statements. The municipality could not provide sufficient appropriate audit evidence to support this balance the municipality's records did not permit for the application of alternative audit procedures.

### **Contingent liabilities**

20. Standards of *Generally Recognised Accounting Practice, GRAP 1, Presentation of financial statements* requires comparative information to be disclosed in respect of the previous period for all amounts reported in the financial statements. The contingent liabilities disclosure note 38 to the financial statements does not have comparative figures in respect of contingent liabilities for the 2009/10 financial accounting period amounting to R4 420 308.

### **Trade and other payables**

21. Standards of Generally Recognised Accounting Practice, GRAP 19, *Provisions, contingent liabilities and contingent assets* requires that a provision be made where the municipality has a present obligation and it is probable that an outflow of resources embodying economic benefits or service potential will be required to settle the obligation. The municipality did not make a provision for the payment of service bonuses amounting to R911 311. The municipality has a practice of paying service bonuses each year. Consequently trade and other payables are understated by R911 311.

22. The district municipality is a water authority in terms of section 84(1)(b) and 84(1)(d) of the

Municipal Structures Act, 1998 (Act No.117 of 1998). The municipality has appointed local municipalities falling within its jurisdiction as service providers in terms of Section 78 of the Municipal Systems Act, 2000 (Act No 32 of 2000). Included in trade and other payables on note 10 to the financial statements, is an amount of R6 258 304 in respect of current year's increase in provision for doubtful debts, in respect of water and sanitation which is a function of the district municipality. The municipality could not provide sufficient appropriate audit evidence to support this balance the municipality's records did not permit for the application of alternative audit procedures.

#### **Revenue**

23. Included in other revenue as per note 21 to the financial statements, is an amount of R1 744 786 in respect of revenue from government grants and subsidies. Consequently, government grants and subsidies revenue in the financial statements is understated by R1 744 786. and other revenue is overstated by the same amount.

#### **Value Added Tax (VAT)**

24. Value Added Tax (VAT) receivable balance of R2 220 100 as disclosed in note 5 to the financial statements, does not agree to my workings of R 3 881 305. The municipality did not reconcile the difference of R1 661 202 between the financial statements and my workings. Consequently, the VAT receivable balance is understated by R1 661 202.

#### **Opinion**

25. In my opinion, because of the significance of the matters described in the Basis for adverse of opinion paragraphs, these financial statements do not present fairly the financial position of the Greater Letaba Municipality as at 30 June 2011 and its financial performance and cash flows for the year then ended, in accordance with South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA).

#### **Emphasis of matter**

26. I draw attention to the matters below. My opinion is not modified in respect of these matters.

#### **Significant uncertainties**

27. With reference to note 36 to the financial statements, the municipality is a defendant in lawsuits amounting to R692 699. The outcome of these lawsuits cannot be presently determined, and no provision for any liability that may result has been made in the financial statements.

#### **Material losses**

28. The municipality suffered a significant loss of 6 640 003 units of electricity with a value of R3 684 265 during the year under review.

## **Additional matters**

### **Unaudited supplementary schedules**

29. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

## **REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS**

30. In accordance with the PAA and in terms of *General notice 1111 of 2010*, issued in *Government Gazette 33872 of 15 December 2010*, I include below my findings on the annual performance report as set out on pages XX to XX and material non-compliance with laws and regulations applicable to the municipality.

### **Predetermined objectives**

#### **Usefulness of information**

31. The reported performance information was deficient in respect of the following criteria:

- Consistency: The reported objectives, indicators and targets are not consistent with the approved integrated development plan.
- Relevance: There is no clear and logical link between the objectives, outcomes, outputs, indicators and performance targets.
- Measurability: The indicators are not well defined, and targets are not specific, measurable, and time bound.

32. The following audit findings relate to the above criteria:

- For the selected programmes, 44% of the planned and reported targets were not measurable in identifying the required performance.
- Reported performance against predetermined targets is not consistent with the approved integrated development plan (IDP) and service delivery budget implementation plan (SDBIP).
- For the selected programmes, 34% of the planned and reported targets were not specific in clearly identifying the nature and the required level of performance.
- For the selected programmes, 37% of the planned and reported targets were not verifiable.

## **Compliance with laws and regulations**

### **Procurement and contract management**

33. Awards were made to providers based on criteria that differed from those stipulated in the original bid documents and were not stipulated in the original bid documents as per the requirements of SCM regulation 21(b) and/or 28(1).
34. Awards were made to providers who are persons in service of other state institutions or whose directors are persons in service of other state institutions in contravention of the requirements of SCM regulations 44. Furthermore the provider failed to declare that he or she is in the service of the state as required by SCM regulation 13(c).
35. Awards were made to suppliers based on preference points that were not allocated and calculated in accordance with the requirements of the Preferential Procurement Policy Framework Act and its regulations.
36. Awards were made to suppliers that did not score the highest points in the evaluation process as per the requirements of section 2(1)(f) of Preferential Procurement Policy Framework Act.
37. Construction contracts were awarded to contractors that did not qualify for the contract in accordance with the prescripts of the Construction Industry Development Board.
38. Sufficient appropriate audit evidence could not be obtained that invitations for competitive bidding were advertised for a required minimum period of days as per the requirements of SCM regulation 22(1) & 22(2).

### **Expenditure Management**

39. The accounting officer did not take reasonable steps to prevent unauthorised, irregular and fruitless and wasteful expenditure, as required by section 62(1) (d) of the Municipal Finance Management Act.

### **Audit committees**

40. The audit committee did not function as required by section 166 of the Municipal Finance Management Act, in that:
  - The audit committee did not review the annual financial statements;
  - The audit committee did not meet at least four times a year.
41. Another committee functioning as the performance audit committee did not perform the following as required by Municipal Planning and Performance Management Regulation 14:
  - meet at least twice during the financial year
  - review the quarterly reports of the internal auditors on their audits of the performance measurements of the municipality
  - review the municipality's performance management system and make recommendations in this regard to the council of the municipality
  - submit an auditor's report to the council regarding the performance management system at least twice during the financial year.

### **Internal audit**

42. Internal audit did not report to the audit committee on matters relating to compliance with the Municipal Finance Management Act, the Division of Revenue Act and other applicable legislation as required by section 165(2)(b) of the Municipal Finance Management Act.
43. The internal audit unit did not function as required by section 165(2) of the Municipal Finance Management Act, in that Internal audit did not advise the accounting officer and report to the audit committee on matters relating to internal audit, internal controls, accounting procedures and practices and loss control.
44. The municipality did not develop and implement mechanisms, systems and processes for auditing the results of performance measurement as part of its internal audit processes as required by section 45(1)(a) of the Municipal Systems Act and Municipal Planning and Performance Management Regulation 14.

### **Asset management**

45. The accounting officer did not take all reasonable steps to ensure that the municipality had and maintained a management, accounting and information system which accounts for the assets of the municipality as required by section 63(2)(a) of the Municipal Finance Management Act.

### **Annual financial statement and annual report**

46. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the Municipal Finance Management Act. Material misstatements identified by the auditors were not corrected, which resulted in the financial statements receiving an adverse audit opinion.
47. The annual performance report did not contain a comparison of the performance of the municipality and of each external service provider with development priorities, objectives and performance indicators set out in its integrated development plan as required by section 46 of the Municipal Systems Act.

### **INTERNAL CONTROL**

48. In accordance with the PAA and in terms of General notice 1111 of 2010, issued in *Government Gazette 33872 of 15 December 2010*, I considered internal control relevant to my audit, but not for the purpose of expressing an opinion on the effectiveness of internal control. The matters reported below are limited to the significant deficiencies that resulted in the basis for adverse opinion, the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

## **Leadership**

49. The management of the municipality did not monitor the effectiveness of the audit committee. The Accounting officer did not review the supply chain management processes of the municipality which led to the municipality incurring irregular expenditure.
50. The accounting officer did not in all instances exercise oversight responsibility over financial reporting.

## **Financial and performance management**

51. The reported objectives, indicators and targets are not consistent with the approved annual performance plan. Performance reports are not reviewed.
52. The CFO did not ensure that amounts disclosed in the financial statements agree to supporting schedules and documents. Accounting standards were incorrectly applied.
53. The work performed by consultants on the assets register and the calculation for the provision of doubtful debts was not reviewed by the CFO.

## **Governance**

54. The audit committee did not review the municipality's financial statements prior to issue to the Auditor – General for auditing. Additionally, the audit committee did not provide oversight over the effectiveness of the internal control environment, including financial and performance reporting and compliance with laws and regulations.
55. The municipality's internal audit did not develop and implement mechanisms, systems and processes for auditing the results of performance measurement as part of its internal audit processes

*Auditor-General.*

Polokwane

30 November 2011



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